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**SASKATCHEWAN
FOREST
PRODUCTS
CORPORATION
1983
ANNUAL
REPORT**







39TH ANNUAL REPORT

SASKATCHEWAN FOREST PRODUCTS CORPORATION

YEAR ENDED OCTOBER 31, 1983





Letter of Transmittal

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Regina, Saskatchewan
February 1, 1984

To His Honour,
The Honourable Frederick W. Johnson,
Lieutenant Governor of the Province of Saskatchewan.

Sir:

I have the honour to submit herewith the annual report of Saskatchewan Forest Products Corporation for the year ended October 31, 1983 including the financial statements therefore, duly certified by the Corporation's auditors and in the form approved by the Treasury Board, all in accordance with The Crown Corporations Act, 1978.

I have the honour to be, Sir,

Your obedient servant,

Neal Hardy,
Minister Responsible,
Saskatchewan Forest Products
Corporation

**Board of Directors**

Honourable Neal Hardy, Chairman — Hudson Bay

Harvey Berg — Weekes

Pat Hill — Saskatoon

Armand Quessy — Debden

Alfred Sauder — Carrot River

Secretary to the Board

Ronald J. Kruzeniski — Regina

Retired from the Board

Honourable George McLeod



Corporation Officers and Management

D. B. Loyd	— General Manager
Donald Neely	— Manager, Finance and Administration
Brian E. Firby	— Manager, Woods
Henry A. Peters	— Manager, Marketing
Paul Klotz	— Manager, Special Projects

Division Management

Rolland N. St. Louis	— Manager, Plywood Division, Hudson Bay
Ernie W. Lawrence	— Manager, Big River Sawmill Division, Big River
Archibald E. Kiteley	— Manager, Carrot River Sawmill Division, Carrot River
Eldon Kerbes	— Manager, Wood Preserving Division, Prince Albert



Report of the General Manager

Introduction

Recovery from the recession in 1982 has been uncertain. Since the extremely poor market conditions in the summer of 1982, lumber sales values increased and peaked in July of 1983. Plywood recovery was slower, caused by the long order file developed to sell inventory in the summer of 1982 and, for this reason, recovery did not really show until November, 1982. Markets were encouraging in the second quarter of 1983 but deteriorated and this downtrend has continued until the end of 1983. Some firming was observed in December.

Since the forest products industry market is allied to housing starts in both U.S. and Canada, the industry benefitted significantly from the housing grants established mid-year both federally and provincially. Although some forecasts indicate a U.S. level of 1.5 million housing starts for 1984, others predict levels of 1.7 million, which will mean some overall improvement in Canadian pricing. Futures markets reflect this in both plywood and lumber. It is anticipated that we will see this improvement starting in the first quarter and this will continue on through summer and bring about improved financial conditions in the company.

The drop in interest rates during 1983 will offer immediate improvement to Saskatchewan Forest Products Corporation, which is highly leveraged. With changes contemplated at the Big River Sawmill operation and changes that have been effected in the past year, it is expected the Corporation will be on a much more solid footing to benefit from the recovery in 1984.

In December 1983 actions were taken to acquire the Northern Forest Operations of the Department of Northern Saskatchewan on January 1, 1984 as a result of the phasing out of the Department of Northern Saskatchewan. These operations are being set up as a separate subsidiary and, based on it being funded by grants to maintain a zero loss position, the subsidiary should have no adverse effect on Saskatchewan Forest Products Corporation.

Assuming that forest products recovery cycles follow traditional patterns, the next two or three years should see a noticeable improvement in the earnings and condition of Saskatchewan Forest Products Corporation but the high debt leverage will continue having an adverse effect on its earnings.

Financial

Lumber markets improved during the year. This increased sales from \$21.3 million in 1982 to \$31.5 million in 1983. In spite of improved sales, the Corporation recorded a loss on operations of \$2,857,000. The write-off of assets of Western Overlay Industries added another \$476,000 to the loss, creating a total loss of \$3,333,000.

A significant item in General Administration and Selling Costs was interest expense. The amount of interest paid on loans for the year was \$2,811,000, which is 8.9% of total sales.

Working capital has been reduced in the past 2 years to a level of \$8,601,000. The Corporation currently is increasing its short-term borrowings to finance inventory build-up.

An inventory write-down of \$157,000 was applied during the year, to the Treating Plant stock. Further reduction of \$434,000 was made to this stock at year end. These reductions give recognition to the fact that slow moving stock exists in the form of fir timbers.

In other locations inventories adjustments both increased and decreased the value of stock. The net value of all inventory adjustments at year end was a reduction of \$398,500.

Capital spending was kept to a minimum for 1983. Total spendings were \$593,000, of which \$239,000 was for major access roads and \$220,000 for completion of the Konus burner at Hudson Bay.



Operations

The Big River Sawmill is being modified by the addition of a small log Cambio debarker and speed control changes to the Chip 'N Saw canter, which will allow this mill to utilize the forest in the western part of the province more effectively. The mill will be able to draw its logs from smaller log diameter stands and this should permit lower pulpwood generation than in the log sizes currently used. Sawmill and Treatment Plant activities are severely handicapped this year by pulpwood quotas that have been placed on pulpwood by the Prince Albert Pulp Co. and these restrictions will affect profitability of all operations until such quotas are removed. The Carrot River Sawmill will continue to operate as it has for the last three or four years; that is, it will remain relatively static until timber allocation strategy for the eastern half of the province is resolved.

The Hudson Bay Plywood Plant is now a much more viable operation than it was in the beginning of 1983 and this has been brought about by significant staff reductions as well as improvements in productivity and supervision. However, the operation will continue to be limited by the quota of peelers available to it and can only gain production from improved recovery. An hydraulic carriage and back stand is being added in this operation, which will improve recovery. However, timing of this addition is in the early part of 1984. Plywood sales are now undertaken by E. Hedlund on the West Coast and this has been a very effective move for resolving some distributor/wholesaling and retailing problems with the project.

The Wood Treatment Plant has had the greatest problem in 1982 and 1983. In 1982 its market for posts vanished and the pole market did not develop as anticipated. In the second and third quarters of 1983 product cost studies were carried out in detail to determine the value of each product. Quotations are now being made on this basis to our various customers. New pole business has been developed with Saskatchewan Power on the basis of new quotations and improved liaison. The company has been approached by major distributors to develop treated lumber for the Ontario market, but it has been extremely difficult to obtain viable wood sources. For this reason the

Corporation is sorting pine at Big River, developing pine logs for cutting at Carrot River, and encouraging contractors to develop pine lumber for the Treatment Plant. These actions will not generate the volume of 12 to 15 mm board feet that may be available in the market for treated wood.

The company continues to have difficulty in obtaining its CSA Certification in spite of bringing in special shipments of plywood from three operators on the West Coast who are assumed to be satisfactory by other treaters. This problem is being aggressively handled and it is hoped that the company will be in a position in the first half of 1984 to deal more confidently with preserved wood foundation material. Although this plant is the largest treating plant in North America, its efforts have been unreliable and irregular since its inception and the corporation is endeavouring to solve the current problems with improved management, better diagnosis of problems, and more effective marketing.

The Retail Lumber Yard operations were closed down this year as being unsatisfactory and uneconomic in the long term. The Prince Albert Retail Lumber Yard was sold and saleable assets in the Sturgis Retail Lumber Yard were also sold.

The corporation's joint venture with Dynamid in the Western Overlay plant at Yorkton has been recognized as a failure and the plant shut down. The plant is leased with an option to buy. Inventory has been removed during this year and should be completely sold in the early part of 1984. Although major equipment suppliers and all the plywood manufacturers in Canada have been approached about a possible purchase of some or all of this equipment, it is considered at this time there is no market for the equipment in view of the closing of some plywood operations on the West Coast. The growing waferboard industry, along with other fibreboard products, has put considerable pressure on the plywood market, but plywood production growth is still positive and should continue to provide a market for the Hudson Bay Plywood Plant. The overlay equipment was moved to Hudson Bay for storage at the year end.

**Employee Relations**

A proposal for selling employees company products at wholesale prices when on major projects was approved in October, 1983.

It is considered that the installation of two new plant managers and a new Industrial Relations Manager at Hudson Bay has improved employee relations significantly. Total number of employees on the active payroll has dropped from 545 to 407.

The following officers left the company in 1983: George McLeod, Director; N. Denmark, General Manager; A. Clark, Special Representative, Promotion and Sales; Al Harris, Manager of Western Overlay Industries and Plywood Sales Manager. D. B. Loyd was brought in as General Manager in March of 1983. Don Neely was brought in as Manager of Finance and Administration in September to replace D. A. Taylor, who accepted a position in the East.

The company must look at its forestry/logging operations when the new rationale is established for the province and studies will continue to further improve each operation. The company's accident prevention record still continues to look poor. The fact that employees on compensation receive 100% recovery of their income and on the Great West Life Benefit program receive 70% contributes significantly to this apparent poor record. It has been statistically shown that absenteeism in a number of compensation cases and length of recovery vary directly as the wage recovery of these employees on such programs.

Labour negotiations were completed in the summer of 1983 and a new memorandum of agreement signed in June. Some substantive changes were made to improve the quality of management in this contract.

This report is respectfully submitted.

D. B. Loyd,
General Manager,
Saskatchewan Forest Products Corporation.

February 1, 1984

AUDITORS' REPORT

To the Members of the Legislative
Assembly of the Province of Saskatchewan

We have examined the statement of financial position of Saskatchewan Forest Products Corporation as at October 31, 1983 and the statements of operations and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the corporation as at October 31, 1983 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Saskatoon, Saskatchewan
December 30, 1983

Price Waterhouse

Price Waterhouse
Chartered Accountants



STATEMENT OF FINANCIAL POSITION

	Note Reference	October 31 1983 1982 (In Thousands)	
ASSETS			
Current assets:			
Cash on deposit		\$ 301	\$ 223
Accounts receivable		4,485	3,512
Inventories	1	8,684	10,556
Prepaid expenses		697	684
		<u>14,167</u>	<u>14,975</u>
Investments	1, 4 & 5	302	953
Other assets	2	372	—
Property, plant and equipment	1 & 6	14,905	15,123
		<u>\$29,746</u>	<u>\$31,051</u>
LIABILITIES AND PROVINCE'S EQUITY			
Current liabilities:			
Accounts payable and accrued		\$ 5,566	\$ 2,171
Long-term notes, less current portion	7	16,831	18,198
Province of Saskatchewan's equity:			
Equity advances from Crown Investments Corporation of Saskatchewan	8		
Deficit	3	20,112	20,112
		12,763	9,430
		<u>7,349</u>	<u>10,682</u>
		<u>\$29,746</u>	<u>\$31,051</u>

(See accompanying notes)



STATEMENT OF OPERATIONS AND DEFICIT

	Note Reference	Year ended October 31	
		1983	1982
		(In Thousands)	
Revenue:			
Sales of forest products		\$31,546	\$21,294
Expenses:			
Operating costs		28,539	26,889
Selling, general and administrative		1,822	1,741
Depreciation and amortization	1	1,140	1,117
Interest on long-term notes	7	2,811	1,730
		<u>34,312</u>	<u>31,477</u>
Loss before the following		2,766	10,183
Share of joint venture loss		91	445
Loss before extraordinary items		2,857	10,628
Extraordinary items	5	476	279
Loss for the year		3,333	10,907
Retained earnings (deficit), beginning of year		(9,430)	1,477
Deficit, end of year		<u>\$12,763</u>	<u>\$ 9,430</u>
(See accompanying notes)			



STATEMENT OF CHANGES IN FINANCIAL POSITION

		Year ended October 31	
	Note Reference	1983	1982
		(In Thousands)	
Working capital provided by:			
Increase in long-term notes — Crown Investments Corporation of Saskatchewan	7	\$ —	\$17,047
Decline in advances to joint venture		84	—
		<u>84</u>	<u>17,047</u>
Working capital applied to:			
Loss for the year before extraordinary item		2,857	10,628
Depreciation and amortization	1	1,140	1,117
Share of joint venture loss		91	445
		<u>1,628</u>	<u>9,066</u>
Total to operations		1,628	9,066
Purchase of property, plant and equipment, net	1 & 6	922	787
Increase in advances to joint venture	1 & 4	—	1,155
Increase in other assets	2	372	—
Reduction of long-term notes	7	1,367	183
		<u>4,287</u>	<u>11,191</u>
Increase (decrease) in working capital		(4,203)	5,856
Working capital, beginning of year		12,804	6,948
Working capital, end of year		<u>\$ 8,601</u>	<u>\$12,804</u>
(See accompanying notes)			



**NOTES TO FINANCIAL STATEMENTS
OCTOBER 31, 1983**

1. Summary of accounting policies:

The following summary of significant accounting policies contains a description of the accounting methods and practices that have an important impact on the corporation's financial statements.

Inventories —

Inventories of logs and mill supplies are valued at the lower of cost and replacement cost. Inventories of lumber, plywood and treated products are valued at the lower of average cost and net realizable value. Average cost includes appropriate production overheads.

Investments —

The corporation follows the equity method in accounting for its investment in a joint venture. The corporation's investment in co-operatives is recorded at cost with dividends being reflected in earnings when received.

Property, plant and equipment —

The costs of maintenance, repairs and minor renewals or replacements are charged to operations as they arise. The cost of major replacements, extensions and improvements are capitalized in the property, plant and equipment accounts. Government grants received in connection with the construction or expansion of production facilities are credited to the cost of such assets. On retirement or disposition of property, plant and equipment, the costs thereof and the related accumulated depreciation are eliminated from the accounts and any gains or losses are reflected in the statement of operations.

Property, plant and equipment are depreciated over their estimated useful lives primarily on the diminishing-balance basis at the following rates:

Buildings	5-10%
Machinery and equipment	6.7 - 10%
Vehicles	15%
Site improvements	4%
Office equipment	10%

2. Other assets:

	October 31	
	1983	1982
	(In Thousands)	
Advances — reforestation dues	\$ 223	\$ —
Agreements receivable	149	—
	<u>\$ 372</u>	<u>\$ —</u>

Advances for the year ended October 31, 1983 consist of payment to the Hudson Bay Reforestation Trust Fund. The original amount paid into the fund was \$592,000 less a subsequent refund of 50% (\$296,000). In the current year, all reforestation dues payable have been applied to reduce the advance. As at October 31, 1983 \$30,000 of the advance has been classified as a prepaid expense.

The agreement receivable relates to the sale of fixed assets at the corporation's Prince Albert Retail Yard. The agreement is to be repaid in 60 blended monthly payments of \$2,283 with the unpaid balance due October 1, 1988. The agreement bears interest at the Bank of Nova Scotia prime lending rate plus 1%. As at October 31, 1983 \$7,200 of the agreement receivable has been classified as a current asset.

3. Status of Saskatchewan Forest Products Corporation:

The corporation was established by Order-in-Council 1899 of 1949 and continues under the provisions of The Crown Corporations Act. These financial statements will be consolidated in the accounts of the Crown Investments Corporation of Saskatchewan.



4. Investments:

	October 31	
	1983	1982
	(In Thousands)	
Investment in and advances to joint venture, see note 5	\$ 297	\$ 948
Investment in co-operatives	5	5
	<u>\$ 302</u>	<u>\$ 953</u>

The corporation has a 51% interest in Western Overlay Industries, an unincorporated joint venture. During the year, the joint venture incurred a loss of \$354,136 which included interest payable to the corporation of \$174,730.

A summary of the financial position of Western Overlay Industries is as follows —

	October 31	
	1983	1982
	(In Thousands)	
Current assets	\$ 56	\$ 297
Fixed assets	250	651
Deposit	(9)	—
	<u>\$ 297</u>	<u>\$ 948</u>
Equity and advances from Saskatchewan Forest Products Corporation	<u>\$ 297</u>	<u>\$ 948</u>

Under the terms of the joint venture agreement, the corporation has a prior claim on the assets of the joint venture to realize any funds it advanced or invested in Western Overlay Industries. The corporation believes that the other joint venturer is in breach of the agreement and legal action has been commenced to attempt to obtain restitution of certain of the losses incurred to date.

5. Extraordinary items:

	October 31	
	1983	1982
	(In Thousands)	
Share of joint venture extraordinary loss:		
Write-down of fixed assets to their anticipated net realizable value	\$ 199	\$ —
Write-down of investment in joint venture to the underlying net asset value	277	279
	<u>\$ 476</u>	<u>\$ 279</u>

In 1982 Western Overlay Industries discontinued operations for an undetermined period. As at October 31, 1983 the discontinuance of operations was deemed permanent and all fixed assets of the joint venture have been written down to their anticipated net realizable value. Accordingly, the corporation has written down the carrying value of its investment in the joint venture to the net realizable value of its underlying assets.



6. Property, plant and equipment:

	October 31	
	1983	1982
	(In Thousands)	
Land	\$ 533	\$ 480
Building and site improvements	5,862	5,889
Roads and spur tracks	3,146	2,549
Machinery and equipment	11,073	10,944
	<u>20,614</u>	<u>19,862</u>
Less: Accumulated depreciation	5,709	4,739
	<u>\$14,905</u>	<u>\$15,123</u>

7. Long-term notes:

	October 31	
	1983	1982
	(In Thousands)	
Crown Investments Corporation of Saskatchewan 10% promissory note repayable in annual instalments of \$83,400. Interest is only payable in years in which the corporation records net earnings.	\$ 1,167	\$ 1,334
Crown Investments Corporation of Saskatchewan promissory note, see below.	16,947	17,047
	<u>18,114</u>	<u>18,381</u>
Less: Portion due within one year classified as current	1,283	183
	<u>\$16,831</u>	<u>\$18,198</u>

As at October 30, 1982 the corporation had borrowed \$15.4 million from Crown Investments Corporation through a series of short-term loans. On October 31, 1982 these short-term loans, together with accrued interest thereon of \$1,647,000, were converted to a 15 year long-term loan. This long-term loan will bear interest at 15% for the first year, with future rates to be negotiated on November 1, 1983 and annually thereafter. Principal repayments will be \$1,200,000 on each October 31 until maturity with the final payment being \$1,347,000. Principal may be repaid prior to maturity without penalty. Interest is due annually.

8. The Province of Saskatchewan's equity:

The Province of Saskatchewan's equity in the corporation is made up of equity advances by the Crown Investments Corporation of Saskatchewan to the corporation since its inception, less amounts repaid or forgiven. These advances are repayable at the discretion of the Crown Investments Corporation of Saskatchewan and do not bear interest. The deficit represents accumulated profits and losses of the corporation since the date of the reorganization on November 1, 1977.

9. Discontinued operations:

In 1983 the corporation discontinued operations at the Prince Albert and Sturgis Retail Yards and all assets were sold during the year.



10. Related party transactions:

Included in these financial statements are income and expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan Crown controlled departments, agencies and corporations with which the corporation is related.

Account balances resulting from these transactions are included in the statement of financial position and are settled on normal trade terms.

Other amounts due to related parties and the terms of settlement are described separately in the financial statements and the notes thereto.

11. Remuneration:

The corporation's six directors received remuneration of \$3,000 (1982 — \$1,500) during the fiscal year. The five senior officers received in aggregate remuneration of \$238,000 for 1983 (1982 — \$266,029).

12. Contingencies:

The corporation, being the defendant to several unresolved statements of claim, has provided for them in its accounts in accordance with advice received from its legal counsel. Any difference which may arise, between amounts provided and amounts experienced, will be accounted for in the period in which the claims are resolved.

13. Subsequent event:

The corporation will be taking over the lumber operations of the Department of Northern Saskatchewan in the 1984 fiscal year. The lumber operations will be incorporated as a subsidiary company, Northern Forest Operations Ltd. The exact terms of the takeover are under negotiation.

14. Comparative figures:

Certain prior year's figures have been reclassified for comparative purposes.

